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STATE OF CONNECTICUT
DEPARTMENT OF REVENUE SERVICES

IP 2004(12)

INFORMATIONAL PUBLICATION

**Q & A on Connecticut Income Tax Changes Affecting
Partnerships and Limited Liability Companies (LLCs) With
Nonresident Partners or Members**

Purpose: This Informational Publication is intended to answer frequently-asked questions concerning new legislation that requires each partnership doing business in Connecticut or having income derived from or connected with sources within Connecticut to pay Connecticut income tax on behalf of its nonresident partners.

For purposes of this publication:

- *Partnership* means and includes a general partnership, limited partnership, limited liability partnership, publicly traded partnership, or limited liability company (LLC) treated as a partnership for federal income tax purposes.
- *Partner* means and includes a partner of a partnership and a member of a LLC treated as a partnership for federal income tax purposes.
- *Publicly traded partnership* means a partnership as defined in I.R.C §7704(b), that is treated as a partnership for federal income tax purposes and that has agreed to file **Form CT-1065/CT-1120SI**, *Connecticut Composite Income Tax Return* (New 12/04).
- *Investing partnership* means a partnership that elects (under 26 C.F.R. §1.761-2) not to be treated as a partnership for federal income tax purposes and thus is not subject to Subchapter K of Chapter 1 of the Internal Revenue Code.
- *Pass-through entity* means and includes an S corporation, general partnership, limited partnership, limited liability partnership, or limited liability company treated as a partnership for federal income tax purposes.

Effective Date: May 6, 2004, and applicable to taxable years of partnerships beginning on or after January 1, 2004.

Statutory Authority: Conn. Gen. Stat. §§12-719(b) and (c) and 12-726, as amended by 2004 Conn. Pub. Acts 216, §§54 and 55.

1. What form is a partnership required to file under the new legislation? For taxable years beginning on or after January 1, 2004, a partnership is required to file **Form CT-1065/CT-1120SI**, where it:

- Is required to file federal Form 1065, U.S. Return of Partnership Income; **and**
- Has any income, gain, loss, or deduction derived from or connected with sources within Connecticut.

Form CT-1065/CT-1120SI is used by all partnerships described above to provide information on the partnership and is also used by partnerships with nonresident partners to make composite payments on behalf of those nonresident partners. Previously, all partnerships were required to file **Form CT-1065**, *Connecticut Partnership Income Tax Return*.

2. When is Form CT-1065/CT-1120SI due? **Form CT-1065/CT-1120SI** is due on or before the fifteenth day of the fourth month following the close of the partnership's taxable year (April 15 for a partnership whose taxable year for federal income tax purposes is the calendar year). If the due date falls on a Saturday, Sunday, or legal holiday, the next business day is the due date.

3. Under what circumstances is a partnership required to make a Connecticut composite income tax payment? A partnership is required to make a Connecticut composite income tax payment on behalf of a partner where:

- The partner's distributive share of the partnership income derived from or connected with Connecticut sources is \$1,000 or more (\$500 or more for publicly traded partnerships);
- An election to be included on a group return (**Form CT-G**, *Connecticut Group Income Tax Return*), has not been made by the partner (see Question 13); **and**
- The partner is a nonresident individual, nonresident trust, nonresident estate, or a pass-through entity.

In accordance with the above criteria, a partnership may be required to make Connecticut composite income tax payments on behalf of all of its partners, some of its partners, or none of its partners.

4. Under what circumstances is a partnership not required to make a Connecticut composite income tax payment? A partnership is not required to make a Connecticut composite income tax payment on behalf of a nonresident partner where:

- The partner's distributive share of the partnership income derived from or connected with Connecticut sources is less than \$1,000 (less than \$500 for a publicly traded partnership); **or**
- An election to be included on a group return (**Form CT-G**) has been made by the partner (see Question 13).

In addition, a partnership is not required to make a Connecticut composite income tax payment where the partner is a resident individual, resident trust, resident estate, real estate investment trust, real estate mortgage investment conduit, regulated investment company, C corporation, or LLC that has elected to be taxed as a corporation for federal income tax purposes.

5. If a partnership makes a Connecticut composite income tax payment on behalf of a nonresident partner, is the partner required to file a Connecticut income tax return? The partner is **not required** to file a Connecticut income tax return if the composite income tax payment made by the partnership on the partner's behalf (and any other composite income tax payment made by any other pass-through entity on the partner's behalf) satisfies the partner's Connecticut income tax liability. The partner is **required** to file a Connecticut income tax return if the composite income tax payment made by the partnership on the partner's behalf (and any other composite income tax payment made by any other pass-through entity on the partner's behalf) does not satisfy the partner's Connecticut income tax liability, or if the partner has Connecticut source income other than from one or more pass-through entities.

6. How are Connecticut composite income tax payments calculated? The Connecticut composite income tax payment for a partner for whom a payment must be made is calculated by multiplying the partner's distributive share of the partnership's separately and nonseparately computed income derived from or connected with Connecticut sources by 5%. The partnership must calculate the Connecticut composite income tax payment based only on the partner's distributive share of income from that partnership derived from or connected with Connecticut sources. The partnership may not take into account any losses that the partner may realize from other sources or Connecticut income tax withholding related to Connecticut employment.

7. When is a partnership required to make estimated Connecticut composite income tax payments for a partner? Beginning with estimated Connecticut composite income tax payments due on or after June 15, 2004, a partnership is required to make *estimated* Connecticut composite income tax payments for a partner where:

- The partnership is required to make a Connecticut composite income tax payment on behalf of the partner (see Question 3); **and**
- The partner's Connecticut income tax liability on the partner's distributive share of the partnership's income derived from or connected with Connecticut sources is expected to equal or

exceed \$1,000. Therefore, estimated Connecticut composite income tax payments will be required if a partner's share of income derived from or connected with Connecticut sources from the partnership is expected to be \$20,000 or more for the taxable year.

In accordance with the above criteria, a partnership may be required to make estimated Connecticut composite income tax payments on behalf of all of its partners, some of its partners, or none of its partners.

For each installment, the partnership must aggregate the estimated Connecticut composite income tax payments made on behalf of nonresident partners and file one **Form CT-1065/CT-1120SI ES**, *Estimated Connecticut Composite Income Tax Payment*.

8. How are estimated Connecticut composite income tax payments calculated? Estimated Connecticut composite income tax payments for a partner for whom an estimated payment must be made are calculated as follows:

- On or before the fifteenth day of the fourth month of the partnership's taxable year (**April 15** for a calendar year partnership), **25%** of the Connecticut income tax liability of the partner must be paid;
- On or before the fifteenth day of the sixth month of the partnership's taxable year (**June 15** for a calendar year partnership), a total of **50%** of the Connecticut income tax liability of the partner must be paid;
- On or before the fifteenth day of the ninth month of the partnership's taxable year (**September 15** for a calendar year partnership), a total of **75%** of the Connecticut income tax liability of the partner must be paid; **and**
- On or before the fifteenth day of the first month of the partnership's next succeeding taxable year (**January 15** for a calendar year partnership), a total of **100%** of the Connecticut income tax liability of the partner must be paid.

For a partnership whose taxable year for federal income tax purposes is other than the calendar year and whose **first** payment for the 2004 taxable year is required to be paid on or after June 15, 2004, such

payment is required to be made on or before the fifteenth day of the fourth month of the partnership's taxable year.

9. What are the "safe harbor" provisions for a partnership making estimated Connecticut composite income tax payments? Estimated Connecticut composite income tax payments for a partner for whom estimated composite income tax payments must be made (see Question 7) are to be made in accordance with Conn. Gen. Stat. §12-722. The required annual payment for the taxable year beginning on or after January 1, 2004, and prior to January 1, 2005, is 90% of the tax shown for the partner on the **2004 Form CT-1065/CT-1120SI**.

The required annual payment for taxable years beginning on or after January 1, 2005, is the lesser of:

- 90% of the tax shown for the partner on the current year **Form CT-1065/CT-1120SI**; or
- 100% of the tax shown for the partner on the prior year **Form CT-1065/CT-1120SI**.

Each required installment is 25% of the required annual payment. In the case of any required installment, if the partner establishes, in accordance with 26 C.F.R. §1.6654-2(d)(2), that the annualized income installment is less than 25% of the required annual payment, the amount of the required installment is the annualized income installment, as described in Conn. Gen. Stat. §12-722(d)(2).

If the required annual payment is not made for a partner, interest at 1% (.01) per month or fraction of a month will be added to the tax due until the earlier of the fifteenth day of the fourth month following the close of the partnership's taxable year, or the date on which the underpayment is paid. The interest may be collected by DRS from either the partnership or the partner.

10. If a partner previously made an estimated Connecticut income tax payment for the 2004 taxable year, may the partnership net that payment against an estimated Connecticut composite income tax payment required to be made on behalf of the partner and pay only the difference to DRS? Yes. The partnership may take into account any estimated Connecticut income tax payment for

the 2004 taxable year made by the partner prior to May 6, 2004.

11. Is a partnership subject to interest and penalty for late payment of the Connecticut composite income tax? Yes. If a Connecticut composite income tax payment reported for a partner on **Form CT-1065/CT-1120SI** is not timely paid, interest will be assessed at 1% (.01) per month or fraction of a month until the tax is paid in full. The penalty for paying all or a portion of the tax late is 10% (.10) of the tax paid late. The late payment penalty may be avoided if the partnership:

- Files **Form CT-1065/CT-1120SI EXT**, *Application for Extension of Time to File Connecticut Composite Income Tax Return*, on or before the original due date of the return;
- Pays at least 90% of the tax shown to be due on the return on or before the original due date; **and**
- Pays the balance due with the return on or before the extended due date.

If the partnership does not file its return and the Commissioner of Revenue Services files a return on its behalf, the penalty for failure to file is 10% (.10) of the balance due or \$50, whichever is greater.

The interest and penalty may be collected by DRS from either the partnership or the partner.

If no tax is due, the Commissioner of Revenue Services may impose a \$50 penalty for the late filing of any return or report that is required by law to be filed.

12. How is a partnership required to notify a partner of the amount of Connecticut composite income tax payments, including estimated Connecticut composite income tax payments, made on behalf of the partner? A partnership will be required to furnish written information, on or before the fifteenth day of the third month following the close of the partnership's taxable year (March 15 for a calendar year partnership), to each partner for whom Connecticut composite income tax payments, including estimated Connecticut composite income tax payments, were made by the partnership during the taxable year.

13. Who may elect to be included in a group return? A partnership doing business in Connecticut, or having income, gain, loss, or deduction derived from or connected with sources within Connecticut, may file **Form CT-G** on behalf of two or more of its qualified electing nonresident partners. All qualified electing nonresident partners must have the same taxable year. Previously, a group return could only be filed by a partnership which had 10 or more qualified electing nonresident partners in a taxable year.

14. Who is a qualified electing nonresident partner for purposes of filing Form CT-G? A *qualified electing nonresident partner* is one who meets all of the following conditions:

- The partner was a nonresident individual for the entire taxable year;
- The partner did not maintain a permanent place of abode in Connecticut at any time during the taxable year;
- The partner (or his or her spouse, if a joint federal income tax return is or will be filed) did not have any income derived from or connected with Connecticut sources other than from one or more pass-through entities;
- The partner waives the right to claim any Connecticut personal exemption under Conn. Gen. Stat. §12-702 and any Connecticut personal credit under Conn. Gen. Stat. §12-703;
- The partner does not have a Connecticut alternative minimum tax liability for the taxable year;
- The partner has the same taxable year as the other qualified electing nonresident partners; **and**
- The partner elects to be included on **Form CT-G**, by completing and delivering to the partnership **Form CT-2NA**, *Connecticut Nonresident Income Tax Agreement/Election to be Included in a Group Return*, prior to the filing of **Form CT-G** by the partnership.

The filing of a group return will be considered to be a group of separate returns meeting the filing requirements otherwise separately imposed on each

qualified electing nonresident partner in the group by DRS. Qualified electing nonresident partners who are included on **Form(s) CT-G** are not required to file **Form CT-1040NR/PY**. DRS retains the right to require the filing of an individual Connecticut income tax return by any of the partners. A nonresident partner may not revoke an election to be included in a group return, or elect to be included in a group return, after the fifteenth day of the fourth month following the close of the entity's taxable year.

15. When is Form CT-G due? **Form CT-G** is due on or before the fifteenth day of the fourth month following the close of the taxable year of the qualified electing nonresident partners (April 15 for calendar year taxpayers). If the due date falls on a Saturday, Sunday, or legal holiday, the next business day is the due date.

16. Are estimated Connecticut group income tax payments required for partners included on Form CT-G? Yes. Estimated Connecticut group income tax payments are required for a partner included on **Form CT-G** if the partner's Connecticut income tax liability on the partner's distributive share of the partnership's income derived from or connected with Connecticut sources is expected to equal or exceed \$1,000. For each installment, the entity must aggregate the estimated Connecticut group income tax payments made on behalf of nonresident partners and file one **Form CT-G ES**, *Estimated Connecticut Group Income Tax Payment*.

17. How does the new legislation affect publicly traded partnerships? A publicly traded partnership is required to report the name, address, social security number, or federal employer identification number to DRS for each unitholder whose distributive share of partnership income derived from or connected with Connecticut sources exceeds \$500.

18. How does the new legislation affect an investing partnership? An investing partnership is not subject to the requirements of the new legislation. However, an investing partnership that does not make the election (under 26 C.F.R. §1.761-2) not to be treated as a partnership for federal income tax purposes, and that is treated as a partnership subject to Subchapter K of Chapter 1 of the Internal Revenue Code, is subject to the requirements of the new legislation.

19. How does the new legislation affect a partnership deemed, pursuant to Conn. Gen. Stat. 12-711(f), not to be carrying on a trade or business in Connecticut? Such a partnership is not subject to the requirements of the new legislation.

20. How does the new legislation affect single member LLCs (SMLLCs)?

- **SMLLC owned by a corporation.** An SMLLC that, for federal income tax purposes, is disregarded as an entity separate from the corporation which is its owner is treated as a C corporation for purposes of the new legislation. Therefore, if the SMLLC is a partner of a partnership, the partnership is not required to make Connecticut composite income tax payments for the SMLLC. Also, the SMLLC is not a pass-through entity, so it is not required to make Connecticut composite income tax payments for its owner.
- **SMLLC owned by an individual.** An SMLLC that, for federal income tax purposes, is disregarded as an entity separate from the individual who is its owner is treated as an individual for purposes of the new legislation. Therefore, if the SMLLC is a partner of a partnership, the partnership is required to make Connecticut composite income tax payments for the SMLLC, if the criteria of Question 3 are met. Also, the SMLLC is not a pass-through entity, so it is not required to make Connecticut composite income tax payments for its owner.
- **SMLLC that elects to be taxed as a corporation.** An SMLLC that elects, for federal income tax purposes, to be taxed as a corporation is treated as a C corporation for purposes of the new legislation. Therefore, if the SMLLC is a partner of a partnership, the partnership is not required to make Connecticut composite income tax payments for the SMLLC. Also, the SMLLC is not a pass-through entity, so it is not required to make Connecticut composite income tax payments for its owner.

21. Does the new legislation require a partnership (“upper-tier partnership”) to make a Connecticut composite income tax payment on behalf of a partner that is itself a pass-through entity (“lower-tier partnership”)? Yes. An upper-tier partnership is required to make a Connecticut composite income tax payment on behalf of a lower-tier partnership where the lower-tier partnership’s share of the upper-tier partnership’s income derived from or connected with Connecticut sources is \$1,000 or more. The upper-tier partnership is also required to make *estimated* Connecticut composite income tax payments on behalf of the lower-tier partnership where the lower-tier partnership’s share of the upper-tier partnership’s income derived from or connected with Connecticut sources would be expected to equal or exceed \$20,000.

However, if both of the following conditions are met, an upper-tier partnership is not required to make a Connecticut composite income tax payment on behalf of a partner of a lower-tier partnership:

- The lower-tier partnership provides sufficient evidence to the upper-tier partnership that the partner of the lower-tier partnership is a person for whom a Connecticut composite income tax payment is not otherwise required to be made (see Questions 3 and 4), for example, the partner is a C corporation or a resident individual; **and**
- Information about the distributive share of the lower-tier partnership owned by the partner is provided to the upper-tier partnership.

Example 1: *L*, a partnership, is a partner of *U*, a partnership. Therefore, *L* is a lower-tier partnership and *U* is an upper-tier partnership. *L*’s distributive share of *U*’s income derived from or connected with Connecticut sources is \$1,000, or more. Each partner of *L* is a C corporation. *L* provides sufficient evidence of this to *U*. *U* is not required to make a Connecticut composite income tax payment on behalf of *L*.

Example 2: The facts are the same as in Example 1 except for the following: *L*’s distributive share of *U*’s income derived from or connected with Connecticut sources is expected to equal or exceed \$20,000, and the partners of *L* are four individuals, each with a 25% distributive share of *L*’s income.

Three of the individuals (*A*, *B*, and *C*) are resident individuals, and one (*D*) is a nonresident individual. *L* provides sufficient evidence of this to *U*. *U* is not required to make a Connecticut composite income tax payment on behalf of *L* with respect to *A*, *B*, or *C*’s distributive share of *L*’s income. *U* is required to make a Connecticut composite income tax payment on behalf of *L*, but only with respect to *D*’s distributive share of *L*’s income. *U* is not required to make estimated Connecticut composite income tax payments on behalf of *L* with respect to *D*’s distributive share of *L*’s income unless it is expected to equal or exceed \$20,000.

Effect on Other Documents: None affected.

Effect of This Document: An Informational Publication addresses frequently asked questions about a current position, policy, or practice, usually in a less technical question and answer format.

For Further Information: Call DRS during business hours, Monday through Friday:

- **1-800-382-9463** (in-state), or
 - **860-297-5962** (from anywhere)
 - **TTY, TDD, and Text Telephone users only** may transmit inquiries anytime by calling 860-297-4911.
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Forms and Publications: Forms and publications are available anytime:

- **Internet:** Preview and download forms and publications from the DRS Web site at **www.ct.gov/DRS**
- **DRS TAX-FAX:** Call **860-297-5698** from the handset attached to your fax machine and select from the menu. (Only forms (not publications) are available on TAX-FAX.)
- **Telephone:** Call **860-297-4753** (from anywhere), or **1-800-382-9463** (in-state) and select **Option 2** from a touch-tone phone.

Paperless Filing Methods (fast, easy, free, and confidential):

- **For business returns:** Use *Fast-File* to file sales and use taxes, business use tax, room occupancy tax, or withholding tax returns over the internet or telephone. Visit the DRS Web site at **www.ct.gov/DRS** and click on *File Returns On-Line*.
- **For resident income tax returns:** Use *WebFile* to file personal income tax returns over the Internet. Visit the DRS Web site at **www.ct.gov/DRS** and click on *File Returns On-Line*.

IP 2004(12)
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Issued: 06/8/2004